

**STATE OF ILLINOIS
ILLINOIS COMMERCE COMMISSION**

Illinois Commerce Commission)	
On Its Own Motion)	
vs.)	
Illinois Bell Telephone Company,)	
Verizon North, Inc. and Verizon South, Inc.)	Docket No. 06-0562
)	
Investigation into the applicability of)	
Section 2-202 of the Public Utilities Act)	
To intrastate coin drop pay telephone)	
Revenues)	

VERIZON’S VERIFIED SURREPLY COMMENTS

Verizon North Inc. and Verizon South Inc. (collectively, “Verizon”), through their attorneys and pursuant to the schedule adopted by the Administrative Law Judge at the November 20, 2006 Status Hearing, hereby submit their Verified Surreply Comments in the above-referenced proceeding.

Introduction

These surreply comments are filed because Staff argued – for the first time on reply – that Section 9-102 of the Illinois Public Utilities Act¹ (“PUA”) requires Verizon to pay Public Utility Fund (“PUF”) taxes on the revenues generated from intrastate coin drop rates for pay telephone services that Verizon provides in Illinois. *See* November 14, 2006 “Reply Comments of the Staff of the Illinois Commerce Commission” (“Staff Reply Comments”) at 2-8. This desperate eleventh-hour argument is merely the latest red herring advanced by Staff in an effort to offset the \$905,318 PUF tax refund due to AT&T Illinois² by generating a new theory of PUF tax liability. Like the other arguments made by Staff over the past two years, the contention that

¹ 220 ILCS 5/9-102.

² *See* November 14, 2006 “Reply Comments of Illinois Bell Telephone Company (Public Version)” (“AT&T Reply Comments”) at 10.

Section 9-102 of the PUA requires the payment of PUF taxes on intrastate coin drop payphone revenues is fatally flawed. Verizon again urges the Commission to resolve this investigation with a conclusive finding that PUF taxes are not appropriately collected on unregulated intrastate coin drop rates for pay telephone services provided in Illinois.

Discussion

I. Section 9-102 of the PUA Does Not Require Verizon to Pay the PUF Tax on Intrastate Payphone Coin Drop Revenues

A. Staff's New Stance on Section 9-102 Is Inconsistent with Its Prior Position That Section 13-501 Is the Origin of the Ostensible "Tariffing Requirement" for Intrastate Coin Drop Payphone Service Rates

Nearly two years ago, Verizon advised the Commission that Section 9-102 of the PUA did not require the payment of PUF tax on revenues from intrastate coin drop payphone service. Verizon did so in response to a letter from the Commission's Financial Information Section demanding remittance of PUF tax on such revenues. *See* December 29, 2004 letter from Philip J. Wood Jr. of Verizon ("Wood Letter") attached as Exhibit B to Verizon's October 17, 2006 Verified Initial Comments ("Verizon Initial Comments"). As noted in the Wood Letter, "[e]ven though payphone and collocation rates can be filed with the Commission, such a filing would not be made under Section 9-102 because there is no requirement that they be filed under that statute." *See* Exhibit B. Staff never responded to the Wood Letter or in any other way sought to refute this point.

In fact, Staff ignored the Wood Letter (as well as similar correspondence from AT&T) for almost two years before the Commission initiated the instant investigation in response to AT&T's pursuit of the \$905,318 PUF tax refund due to it. In its August 16, 2006 initiating Order, the Commission made an August 1, 2006 "Telecommunications Division Staff Report" ("Staff Report") regarding PUF tax liability on intrastate coin drop rates for pay telephone

services provided in Illinois part of the record of this docket. *See* Order at 3. *Neither the initiating Order nor the Staff Report referenced Section 9-102 of the PUA* as the basis for Verizon's and AT&T's alleged liability for PUF tax payments on intrastate coin drop pay telephone revenues collected by those companies, despite the fact that the legal issue had been raised by Verizon nearly two years prior. Rather, Staff has consistently asserted that the ostensible tariffing requirement that triggered the alleged PUF tax liability arose under Section 13-501 of the PUA, not Section 9-102. *See* Verizon Reply Comments at 6. Of course, as AT&T has noted in its earlier filings in this docket (and supported by affidavit), the Commission's Office of General Counsel long ago disagreed with Staff on this point, and instead concurred with AT&T that there was no tariffing requirement relating to intrastate coin drop pay telephone services. *See* October 17, 2006 "Comments of Illinois Bell Telephone Company" ("AT&T Initial Comments") at 4; AT&T Reply Comments at 8-9.

At the August 30, 2006 status hearing in this proceeding, Staff requested the opportunity to supplement the Staff Report by filing verified comments on October 17, 2006 (the same day Verizon and AT&T were required to respond to the Staff report). Despite the nearly two years that had passed since the Commission received the Wood Letter, Staff once again made no assertion that Section 9-102 was the basis of Staff's theory of liability. Only after Verizon noted that Staff had *never* made such an argument, and pointed out that this was fatal to Staff's position, did Staff do so for the first time on reply. *See* Staff Reply Comments at 2-8.

B. Section 9-102 of the PUA Does Not Apply to Deregulated Intrastate Coin Drop Rates for Pay Telephone Services Provided in Illinois

As both Verizon and AT&T have amply demonstrated, the FCC has definitively deregulated the rates that providers charge for local payphone service. *See* First Report and Order, *Implementation of the Pay Telephone Reclassification and Compensation Provisions of*

the Telecommunications Act of 1996, CC Docket No. 96-388 (rel. September 20, 1996) at ¶¶ 51-61 (“*Payphone Order*”); and Order on Reconsideration, *In the Matter of Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996 et al.*, FCC 96-439/CC Docket Nos. 91-35/96-128 (rel. November 8, 1996) at ¶ 143-147 (“*Payphone Reconsideration Order*”). On appeal, the D.C. Circuit unequivocally affirmed these orders, finding that the FCC “has been given an express mandate to preempt State regulation of local coin calls.” *See Illinois Public Telecommunications Ass’n v. FCC*, 117 F.3d 555, 563 (D.C. Cir. 1997).

Even Staff does not dispute that the Commission may not set, review, or otherwise regulate intrastate coin drop pay telephone rates, recognizing that “federal law removed state authority to set prices for local coin calls from pay telephones” and conceding that “the Commission may not regulate the *price* for intrastate local coin pay telephone service....” *See* Staff Reply Comments at 2 (*Italics in original*). As a consequence, these rates are not subject to regulation under Article IX of the PUA, which governs only *regulated rates*. As Verizon explained in its Reply Comments, statutory tariffing and rate approval requirements such as those set forth in Article IX are the hallmark example of rate regulation. *See Citizens Utility Board v. Illinois Commerce Commission*, 655 N.E.2d 961, 967 (Ill. App. 1st Dist. 1995) (“*CUB*”) (“[t]hese plenary requirements embody the Commission’s plenary jurisdiction to regulate public utilities with respect to the reasonableness of rates.”); *see also Chicago SMSA L.P. v. Illinois Dept. of Revenue*, 715 N.E.2d 724 (Ill. App. 1st Dist. 1999) (“*Illinois DOR*”) (describing “rate and market entry regulation” as “heart of regulation”). Staff attempts, unconvincingly, to argue that “Section 9-102 is not limited to regulated prices” (Staff Reply Comments at 3), but the

provisions of Section 9-102 quoted by Staff only confirm that the statute's purpose is regulating rates and any associated rate-affecting terms and conditions of service.

The Commission cannot ignore (as does its Staff) that the formal title of Article IX of the PUA is "RATES," and that rate regulation is the fundamental purpose of Article IX. Section 9-101 explicitly mandates that the rates subject to Article IX be "just and reasonable." *See* 220 ILCS 5/9-101. Subsequent sections of Article IX confirm that the rates required to be filed and published thereunder are subject to ICC review and approval; may not be changed without 45 days notice to the ICC; and are subject to suspension pending a hearing on the "propriety" thereof. *See, e.g.*, 220 ILCS 5/9-104 and 9-201(b). Staff's argument that unregulated rates are somehow subject to the rate regulation requirements of Article IX turns the whole concept of regulation on its head. In sum, Staff's contention that the rate regulation provisions of Article IX apply to the deregulated rates for intrastate coin drop pay telephone services in Illinois is specious.

C. Section 9-102 of the PUA Does Not Convert Intrastate Coin Drop Pay Telephone Revenues Into "Gross Revenues" Under Section 3-121

Staff makes the contorted argument that revenues derived from intrastate coin drop pay telephone services provided in Illinois are subject to the PUF tax because Verizon "collect[s] revenue pursuant to the *classifications* which [it is] required to file under Section 9-102 of the PUA." *See* Staff Reply Comments at 2. The essence of Staff's argument is that because Verizon's local payphone services are "classified" as competitive services, the revenues therefrom are collected due to the "classification" of those services as competitive. The next step in Staff's logic is that since competitive services are classified in Article XIII of the PUA, and Section 13-503 references the filing requirements of Section 9-102, Verizon's intrastate coin drop pay telephone revenues are collected under "classifications" it is required to file under

Section 9-102.³ Rounding out Staff's theory is that since these revenues are collected pursuant to Section 9-102's filing requirement, they meet Section 3-121's definition of "gross revenues," and are consequently subject to the PUF tax under Section 2-202.

Staff's creative statutory "daisy chain" is fatally flawed. Staff ignores that intrastate coin drop pay telephone rates are deregulated, and therefore not subject to the rate regulation provisions of Article IX of the PUA regardless of Section 13-503's internal reference to filing processes outlined in Section 9-102. Staff also fails to recognize the critical distinction between Section 13-503 referring to the filing provisions of Section 9-102, and the unreasonable leap that Staff makes in asserting that Section 9-102 is therefore fully applicable to services like those at issue here, even though the rates for those services are not subject to regulation.

Even if the Commission is inclined to entertain Staff's sudden shift in position that the ostensible "informational tariffing requirement" for intrastate coin drop payphone services arises not out of Section 13-501 (as the Commission has posited for more than a decade), but under some combination of Sections 13-503 and 9-102, revenues from competitive services are not, by virtue of Section 13-503's internal reference to Section 9-102, "collected" pursuant to filings required by Section 9-102. If they are "collected" pursuant to any alleged filing requirement (the existence of such a requirement both Verizon and AT&T hotly dispute, with concurrence from the Commission's Office of General Counsel), it would be pursuant to a filing required by Section 13-503. In other words, the mere fact that Section 13-503 incorporates filing parameters set forth in Section 9-102 does not translate into a requirement that rates for intrastate coin drop

³ Staff claims that AT&T agrees with Staff's contention in this regard. Staff Reply Comments at 5. An actual review of AT&T's words demonstrates that AT&T merely confirmed that Section 9-102 sets forth a tariffing requirement to which "**regulated** rates and charges of telecommunications services are subject to 13-503 of the PUA." *Id.* (Italics added). Staff ignores that AT&T has consistently argued throughout this proceeding that intrastate coin drop payphone rates are **deregulated** and therefore not subject to this requirement. Moreover, footnote 2 to AT&T's Reply Comments plainly states that "[e]ven if the Commission were to conclude that it has authority to impose an informational-only tariff requirement on non-regulated rates (and it does not), such authority clearly does not emanate from Section 9-102." See AT&T Reply Comments at 8, FN 2.

payphone service be filed *pursuant to Section 9-102*. Section 9-102 requires only the filing of rates *regulated* under Article IX of the PUA. Moreover, even if the legislature had intended to subject *all* rates for *all* services to the rate regulation requirements of Section 9-102 (including filing a schedule of regulated rates) by referencing that filing process in Section 13-503, the FCC has preempted it from doing so. The only rates required to be filed under Section 9-102 are those subject to regulation by the Commission for their compliance with the “just and reasonable” standard. Intrastate coin drop payphone rates do not meet this condition – as Staff has conceded – because they are not subject to any regulation. Accordingly, revenues from local coin pay telephone service are not collected pursuant to rates required to be filed under Section 9-102.

Consequently, PUF taxes cannot be due on the revenues derived from the intrastate coin drop pay telephone services Verizon provides in Illinois, since those revenues do not qualify as “gross revenues,” as defined in Section 3-121 of the PUA. The relevant portions of the statutory definition of “gross revenue” bear reiteration:

As used in Section 2-202 of this Act, the term “gross revenue” includes all revenue which (1) is collected by a public utility subject to regulations under this Act (a) pursuant to the rates, other charges, and classifications which it is required to file under Section 9-102 of this Act and (b) pursuant to emergency rates as permitted by Section 9-104 of this act, and (2) is derived from the intrastate public utility business of such a utility.⁴

In other words, to be subject to the PUF tax, revenues must be “*collected ... pursuant to the rates, other charges and classifications* which [a public utility] is required to file under Section 9-102 of this Act.” Staff attempts to deflect the import of these words by focusing the Commission’s attention solely on the word “classifications,” rather than the phrase “rates, other charges and classifications” as a cohesive unit. Staff asserts, without any basis, that the term

⁴ 220 ILCS 5/3-121.

“classifications” refers to the competitive and non-competitive *service* classifications of Article XIII of the PUA, rather than *rate* classifications that arise under Article IX – *e.g.*, business, residential, etc. *See* Staff Reply Comments at 3.⁵ It is Verizon’s understanding that AT&T’s surreply comments will explain that the term “classifications” in Article IX dates back many decades prior to the enactment of Section 13-502 of the PUA, which states that telecommunications services will be classified as competitive or non-competitive. Given that Article IX deals with rates, whereas Article XIII deals with competitive/non-competitive services and was enacted years later, the only logical interpretation of the reference to “classifications” in the context of Section 9-102 is that it refers to *rate* classifications, not to competitive and non-competitive *service* classifications.

Verizon’s intrastate coin drop payphone revenues are therefore not “collected” pursuant to “rates, other charges and classifications” required to be filed under Section 9-102 of the PUA. Moreover, under Section 3-120 of the PUA, “intrastate public utility business” of a utility is limited to public utility business over which the Commission has *jurisdiction*. Thus, several requirements of Section 3-121’s definition of “gross revenues” cannot be satisfied here.

The Illinois Appellate Court has unambiguously determined that revenues excluded from the definition of “gross revenues” cannot be subject to the PUF tax:

Because the petitioners’ services do not generate any “gross revenue” as that term is defined in section 3-121, it is clear that they have no tax liability under section 2-202 of the Act. Accordingly, we hold that the petitioners are not obligated to pay public utility tax on the revenue generated by their cellular services.⁶

⁵ Earlier in its Reply Comments, Staff chooses to ignore altogether the portion of the definition of “gross revenues” that relates to Section 9-102, identifying only portion of Section 3-121 that mandates that “gross revenues” be “derived from the intrastate public utility business of [a public] utility,” without mentioning that they must also be collected pursuant to “rates, other charges and classifications” required to be filed under Section 9-102. *See* Staff Comments at 1.

⁶ *See Chicago SMSA Limited Partnership v. Illinois Commerce Commission*, 672 N.E.2d 37, 39 (Ill. App. 3rd Dist. 1996) (“*Chicago SMSA*”).

In its subsequent decision in *Illinois DOR*, the Illinois Appellate Court reiterated that the *Chicago SMSA* decision had held that cellular service providers bore no PUF tax liability under the PUA because they were excluded from rate regulation. *See Illinois DOR* at 724.

D. Section 745.20 of the Commission's Rules Is Irrelevant

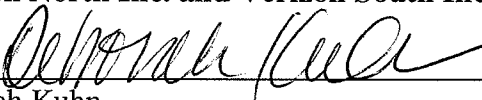
Staff's effort to conjure up a new, non-statutory basis for its ostensible "informational filing requirement" by relying on 83 Ill. Admin. Code § 745.20 is unavailing. The reach of that rule is necessarily limited to those matters over which the Commission has jurisdiction. The FCC has preempted the Commission's authority to regulate intrastate coin drop payphone rates, including the Commission's authority to require them to be tariffed. The Illinois Appellate Court has confirmed that tariffing requirements exist to allow for regulation of rates. *See Chicago SMSA, supra*. Since the Commission cannot regulate intrastate coin drop payphone rates, it cannot require them to be tariffed, notwithstanding Staff's bold assertion that detariffing cannot occur absent a Commission order. Indeed, any contention that the Commission must first issue an order acknowledging that preemption has occurred before preemption can occur is simply unsupportable. 47 U.S.C. § 276(c) states unequivocally that "[t]o the extent that any State requirements are inconsistent with the [Federal Communication's] Commission's regulations, the Commission's regulations on such matters shall preempt such State requirements." Staff's "it's not preempted until *we say* it's preempted" stance is incorrect as a matter of law.

Conclusion

Verizon again urges the Commission to reject Staff's efforts to collect PUF tax on revenues from Verizon's unregulated intrastate coin drop pay telephone services. Staff's new-found theories contort the proper application of Sections 13-503 and 9-102 of the PUA, and cannot support Staff's claims that PUF taxes are due on those revenues. For all the reasons discussed herein and in Verizon's earlier comments, the Commission should close this investigation with a conclusive finding that PUF taxes are not appropriately collected on such revenues.

Dated: December 6, 2006

Verizon North Inc. and Verizon South Inc.

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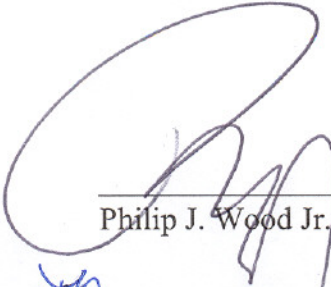
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Docket No. 06-0562

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)
COUNTY OF McLEAN)

VERIFICATION

Philip J. Wood Jr., being duly sworn, states on oath that he is Verizon's Vice President of Public Affairs, Policy & Communications for Illinois, and that the factual statements made in the foregoing "Verizon's Verified Sureply Comments" are complete and accurate to the best of his knowledge, information and belief.


Philip J. Wood Jr.

Subscribed and sworn to before me this 4th day of December 2006.





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NOTICE OF FILING

Please take notice that on December 6, 2006, I caused the foregoing "Verizon's Verified Surreply Comments" in the above-captioned matter to be filed electronically with the Illinois Commerce Commission via its E-Docket system.



Deborah Kuhn

CERTIFICATE OF SERVICE

I, Deborah Kuhn, certify that I caused the foregoing "Verizon's Verified Surreply Comments," together with a Notice of Filing, to be served upon all parties on the attached service list on this 6th day of December, 2006, by electronic mail.



Deborah Kuhn

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DOCKET NO. 06-0562**

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